Report

of the

Examination of

Holland Mutual Fire Insurance Company

Cedar Grove, Wisconsin

As of December 31, 2004

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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August 26, 2005

Honorable Jorge Gomez
Commissioner of Insurance
State of Wisconsin
125 South Webster Street
Madison, Wisconsin 53702

Commissioner:

In accordance with your instructions, an examination has been performed as of December 31, 2004, of the affairs and financial condition of:

HOLLAND MUTUAL FIRE INSURANCE COMPANY
Cedar Grove, Wisconsin

and the following report thereon is respectfully submitted:

I. INTRODUCTION

The previous examination of Holland Mutual Fire Insurance Company (the company) was made in 2001 as of December 31, 2000. The current examination covered the intervening time period ending December 31, 2004, and included a review of such subsequent transactions deemed essential to complete this examination.

The "Summary of Examination Results" contains elaboration on all areas of the company's operations. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The company was organized as a town mutual insurance company in June 1870, under the provisions of the then existing Wisconsin Statutes. The original name of the company was the Town Holland Farmers Mutual Insurance Company. Subsequent amendments to the company's articles and bylaws changed the company's name to that presently used.

During the period under examination, there were no amendments to the articles of incorporation or the bylaws.

The company is currently licensed to write property, including windstorm and hail, and nonproperty insurance. The company is currently licensed to write business in the following counties: Ozaukee, Sheboygan, and Washington.

A review was made of the policy and application forms currently used by the company. The company issues approved policies with or without endorsements for terms of one year with premiums payable on the advance premium and assessment basis. The company also charges a policy fee equal to $25 for active farmowners, $15 for fire and extended coverage, $10 for homeowners, and $5 for rental.

Business of the company is acquired through eight agents, three of whom are directors of the company. Agents are presently compensated for their services as follows:

Type of Policy	**Compensation**
New and Renewal business	15%

Losses are adjusted by the secretary or the president and approved by the adjusting committee. Adjusters receive $10 to $20 for each loss adjusted, depending on how far the travel is and how long it takes to adjust the loss. No travel allowance is provided.

Policyholders may participate in the management and control of the company by attending and voting at all annual or special meetings of the members. No member may vote by proxy. The annual meeting of the company for the election of directors and special meetings of the company are held in accordance with its articles of incorporation.

Board of Directors

The board of directors consists of six members divided into three classes. One class is elected at each annual meeting for a term of three years. Vacancies on the board may be filled by the directors for the interim to the next annual meeting when a director shall be chosen for the unexpired term.

The current board of directors consists of the following policyholders of the company:

Name	Principal Occupation	Residence	Expiry
Marvin Potter*	Shuttle bus driver	Oostburg, Wisconsin	2008
Lamont Risseeuw	Retired	Cedar Grove, Wisconsin	2008
Larry Bares*	Rural mail carrier	Belgium, Wisconsin	2006
Jerome Grotenhuis*	Farmer	Cedar Grove, Wisconsin	2006
Lloyd Ter Maat	Carpenter	Cedar Grove Wisconsin	2007
Stanley Lammers	Farmer	Oostburg, Wisconsin	2007

Directors who are also agents are identified with an asterisk.

Members of the board currently receive $50.00 for each meeting attended and $0.375 per mile for travel expenses.

Officers

Officers are elected by the board of directors from among its members and hold office for one year or until their successors are duly elected and qualified. Officers serving at the present time are as follows:

Name	Office	2004 Salary
Lloyd Ter Maat	President	$ 900
Marvin Potter	Vice President	9,692*
Jerome Grotenhuis	Secretary	36,725**
Lamont Risseeuw	Treasurer	1,500

* Commissions.
** Includes $14,635 of commissions.

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The committees at the time of the examination are listed below:

Adjusting Committee
Lloyd Ter Maat, Chair
Lamont Risseeuw
Stanley Lammers
Marvin Potter
Larry Bares
Jerome Grotenhuis

Investment Committee
Lloyd Ter Maat, Chair
Lamont Risseeuw
Stanley Lammers

Growth of Company

The growth of the company since the previous examination as compiled from its filed annual statements was as follows:

Year	Net Premiums Earned	Policies In Force	Net Income	Admitted Assets	Policyholders' Surplus
2004	$201,562	1,251	$ 36,832	$515,661	$304,462
2003	166,128	1,270	(29,120)	463,022	247,825
2002	122,399	1,320	(79,418)	494,587	280,709
2001	116,964	1,119	(59,234)	524,638	374,597
2000	119,971	1,063	(58,659)	568,919	433,055

The ratios of gross and net premiums written to surplus as regards policyholders since the previous examination were as follows:

Year	Gross Premiums Written	Net Premiums Written	Ending Surplus	Writings Ratios Gross	Writings Ratios Net
2004	$388,952	$209,517	$304,462	128%	69%
2003	363,370	191,352	247,825	147	77
2002	315,785	156,838	280,709	112	56
2001	243,996	124,871	374,597	65	33
2000	230,861	129,890	433,055	53	30

For the same period, the company's operating ratios were as follows:

Year	Net Losses and LAE Incurred	Other Underwriting Expenses Incurred	Net Earned Premiums	Loss Ratio	Expense Ratio	Com-posite Ratio
2004	$ 75,082	$110,840	$201,562	37%	53%	90%
2003	83,908	118,625	166,128	51	62	113
2002	99,258	177,331	122,399	81	75	156
2001	95,983	100,508	116,964	82	80	163
2000	114,105	89,415	119,971	95	69	164

In 2004, the company experienced a positive net underwriting result of $15,640, the first such result over the last ten years, and net income of $36,832, the only year of positive net income during the period under examination.

The company’s net underwriting expense ratio has been as high as 36 percentage points greater than the average for the Wisconsin town mutual industry as a whole in 2001 and during the period under examination it has averaged 25 percentage points greater than the Wisconsin town mutual average. In 2004, the company was 12 percentage points over the average, which indicates improvement, but this improvement will need to be continued and sustained for the company to continue independently.

With the exception of 2004, the company's net loss and loss adjustment expense ratio was at or above the industry average for all Wisconsin town mutuals during the period under examination. In 2004, the company's net loss and loss adjustment ratio was 14 points below the industry average. In 2001 and 2002 the company reported a net loss of $59,234 and $79,418, respectively, due to wind and lightning storms. In 2003, the net loss of $29,120 was attributed to one significant fire claim which caused the losses paid to almost double from the level of losses typically paid by the company. The industry average for all Wisconsin town mutuals indicated a net loss in 2001 and underwriting losses in 2001 and in 2002.

II. REINSURANCE

The examiners' review of the company's reinsurance portfolio revealed there is currently one ceding treaty. The treaty contained a proper insolvency clause and complied with s. Ins 13.09 (3), Wis. Adm. Code, concerning maximum wind loss. Company retentions of risk complied with s. Ins 13.06, Wis. Adm. Code.

	Reinsurer:	Wisconsin Reinsurance Corporation
	Effective Date:	January 1, 2005
	Termination provisions:	Either party may terminate the contract as of January 1, 2006, or any subsequent January 1, by giving to the other party at least 90 days' advance notice in writing.
1.	Type of contract:	Class A Excess of Loss Reinsurance
	Lines reinsured:	All liability (nonproperty) business
	Company's retention:	$500 for each and every loss occurrence. The reinsurer may permit the company to adjust property damage losses that fall within the company's net loss retention.
	Coverage:	100% of loss and loss adjustment expense in excess of the company's retention up to the following maximum policy limits: $1,000,000 – per occurrence, single limit, combined for bodily injury and property damage liability. $1,000,000 – split limits, in any combination of bodily injury and property damage liability. $5,000 – for medical payments, per person; $25,000 per accident.
	Reinsurance premium:	75% of the premium written for each and every policy of the business covered.
2.	Type of contract:	Class B First Surplus Reinsurance
	Lines reinsured:	Property
	Company's retention:	When the company's net retention is $150,000 or more, the company may cede on a pro rata basis up to $800,000. When the net retention is $150,000 or less, the company may cede up to 50% of such risk. Annual aggregate deductible equal to 10% of the loss and loss adjusting expenses.
	Coverage:	Pro rata share of each and every loss, including loss adjustment expense, corresponding to the amount of the risk ceded.

	Reinsurance premium:	Pro rata portion of all premiums, fees and assessments corresponding to the amount of each risk ceded.
	Ceding commission:	Commission allowance: 15% of the premium paid. Profit commission: up to 15% of the reinsurer's net profit.
3.	Type of contract:	Class C-1 First Layer Excess of Loss Reinsurance
	Lines reinsured:	Property
	Company's retention:	$20,000 for each and every risk resulting from one loss occurrence.
	Coverage:	100% of any loss, including loss adjustment expenses, in excess of $20,000 up to a maximum of $40,000 in respect to each and every loss occurrence.
	Reinsurance premium:	The rate in effect shall be determined by taking the sum of the four years' losses incurred (paid plus outstanding) by the reinsurer divided by the total of the net premiums written for the same period, multiplied by the factor 100/80ths, subject to a maximum rate of 18% and a minimum rate of 7%. The current effective rate is 8.01%. The current deposit premium is $26,593, subject to a minimum premium of $20,000.
4.	Type of contract:	Class C-2 Second Layer Excess of Loss Reinsurance
	Lines reinsured:	Property
	Company's retention:	$60,000 for each and every loss occurrence.
	Coverage:	100% of any loss, including loss adjustment expenses, in excess of $60,000 for each and every risk resulting from one loss occurrence up to a maximum of $90,000 in respect to each and every loss occurrence.
	Reinsurance premium:	7% of the current net premiums written. Deposit premium: $23,240 Minimum premium: $17,000
5.	Type of contract:	Class D/E-1 First Aggregate Stop Loss Reinsurance
	Lines reinsured:	Property and nonproperty
	Company's retention:	Net losses, including loss adjustment expenses, up to 65% of the company's net premium written; subject to a minimum retention of $170,000.

Coverage:	100% of annual aggregate losses, including loss adjustment expenses, exceeding 65% of net premium written and in excess of the company’s retention.
Reinsurance premium:	The rate for each annual period shall be determined by taking the sum of the eight years’ losses incurred by the reinsurer divided by the total of the net premiums written for the same period multiplied by the factor of 100/80ths, subject to a maximum rate of 25% and a minimum rate of 6%. Current rate: 9.21% Deposit premium: $32,304 Minimum premium: $25,000

III. FINANCIAL DATA

The following financial statements reflect the financial condition of the company as reported to the Commissioner of Insurance in the December 31, 2004, annual statement. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Policyholders' Surplus."

Holland Mutual Fire Insurance Company
Statement of Assets and Liabilities
As of December 31, 2004

Assets	Ledger	Nonledger	Not Admitted	Net Admitted
Cash deposited in checking account	$ 87,436	$	$	$ 87,436
Cash deposited at interest	265,000			265,000
Stocks and mutual fund investments	95,903			95,903
Real estate	34,948			34,948
Premiums, agents' balances and installments:				
In course of collection	26,291			26,291
Investment income accrued		6,083		6,083
Other nonadmitted assets:				
Furniture and Fixtures	2,544		2,544	
Prepaid Expenses	453		453	
Totals	$512,575	$6,083	$2,997	$515,661

Liabilities and Surplus

Net unpaid losses	$ 8,580
Unpaid loss adjustment expenses	600
Commissions payable	3,760
Fire department dues payable	239
Unearned premiums	187,755
Reinsurance payable	6,048
Amounts withheld for the account of others	1,094
Payroll taxes payable (employer’s portion)	305
Other liabilities:	
Expense-related:	
Accounts payable	210
Accrued property tax	2,608
Total Liabilities	211,199
Policyholders' surplus	304,462
Total Liabilities and Surplus	$515,661

Holland Mutual Fire Insurance Company
Statement of Operations
For the Year 2004

Net premiums and assessments earned		$201,562
Deduct:		
Net losses incurred	$ 67,385	
Net loss adjustment expenses incurred	7,697	
Other underwriting expenses incurred	110,840	
Total losses and expenses incurred		185,922
Net underwriting gain (loss)		15,640
Net investment income:		
Net investment income earned	6,739	
Net realized capital gains	3,993	
Total investment gain (loss)		10,732
Other income (expense):		
Policy Fees	10,460	
Total other income		10,460
Net Income (Loss)		$ 36,832

Holland Mutual Fire Insurance Company
Reconciliation and Analysis of Surplus as Regards Policyholders
For the Four-Year Period Ending December 31, 2004

The following schedule is a reconciliation of surplus as regards policyholders during the period under examination as reported by the company in its filed annual statements:

	2004	**2003**	**2002**	**2001**
Surplus, beginning of year	$247,825	$280,709	$374,597	$437,268
Net income	36,832	(29,120)	(79,418)	(59,234)
Net unrealized capital gains or (losses)	19,371	(4,198)	(15,965)	(3,797)
Change in nonadmitted assets	434	434	1,495	360
Surplus, end of year	$304,462	$247,825	$280,709	$374,597

Reconciliation of Policyholders' Surplus

A reconciliation of the policyholders' surplus as reported by the company in its filed annual statement and as determined by the examination is detailed in the following schedule:

Policyholders' surplus per December 31, 2004, annual statement			$304,462
Item	**Increase**	**Decrease**	
Reinsurance Payable	$3,200	$	
Reinsurance Commission Receivable	4,960		
Total	$8,160	$	
Increase to Surplus per Examination			8,160
Policyholders' Surplus per Examination			$312,622

Examination Reclassifications

	Debit	**Credit**
Premiums Deferred and Not Yet Due	$4,830	$
Premiums in Course of Collection		4,830
Total reclassifications	$4,830	$4,830

IV. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

Comments and recommendations contained in the last examination report and the action taken on them by the company are as follows:

1. Underwriting—It is suggested that the company include photos of the insured properties with their policy file and that this step be included in the inspection procedure for both new and renewal business.

   Action—Partial compliance. See comments in the summary of current examination results.

2. Transition Into the New Investment Rule—It is recommended that the company make no additional Type 2 investments until the company meets the required amount of Type 1 investments, pursuant to s. Ins 6.20 (6) (c), Wis. Adm. Code.

   Action—Compliance.

3. Stocks and Mutual Funds Investments—It is recommended that the company retain all stock certificates or other evidence of ownership.

   Action—Compliance.

4. Premiums, Agents' Balances, and Installments Booked but Deferred and Not Yet Due—It is recommended that the company calculate and record deferred premiums in accordance with the Town Mutual Annual Statement Instructions.

   Action—Noncompliance. See comments in the summary of current examination results.

5. Net Unpaid Losses—It is recommended that the company keep a file for all claims including claims closed without payment in compliance with s. Ins 6.80 (4), Wis. Adm. Code.

   Action—Compliance.

6. Net Unpaid Losses—It is recommended that the company obtain a signed proof of loss for each claim submitted and keep the proof of loss with the claim file; or the board of directors should set a threshold upon which a signed proof of loss would be required and maintained in the claim file.

   Action—Compliance.

7. Net Unpaid Losses—It is recommended that the company record all reinsurance recoverables in the loss register and in the claim file.

   Action—Compliance.

8. Unpaid Loss Adjustment Expenses—It is recommended that the company establish a logical methodology in determining unpaid loss adjustment expenses such as one based on historical figures.

   Action—Noncompliance. See comments in the summary of current examination results.

Current Examination Results

Corporate Records

The minutes of the annual meetings of policyholders and meetings of the board of directors and committees thereof were reviewed for the period under examination and also for the subsequent period.

Biographical data relating to company officers and directors have been reported in accordance with the provisions of s. Ins 6.52, Wis. Adm. Code.

The company has executed formal written agreements with its agents. The contracts include language indicating the agent will represent the company's interests "in good faith."

Conflict of Interest

In accordance with a directive of the Commissioner of Insurance, each company is required to establish a procedure for the disclosure to its board of directors of any material interest or affiliation on the part of its officers, directors, or key employees which conflicts or is likely to conflict with the official duties of such person. A part of this procedure is the annual completion of a conflict of interest questionnaire by the appropriate persons. The company has adopted such a procedure for disclosing potential conflicts of interest. Conflict of interest questionnaires were reviewed for the period under examination with no apparent conflicts being noted.

Fidelity Bond and Other Insurance

The company is afforded coverage under the terms of the following bonds or contracts and has complied with s. Ins 13.05 (6), Wis. Adm. Code, which sets forth the minimum requirements for fidelity bond coverage:

Type of Coverage	Coverage Limits
Fidelity Bond	
Treasurer, Secretary and President	$ 35,000 each
Directors and Officers Liability, Company Professional Liability	500,000
Property Coverage	
Building	99,633
Personal property	7,116

Underwriting

The company has a written underwriting guide. The guide covers all the lines of business that the company is presently writing. The company has a formal inspection procedure for new business; however, no inspection procedure is in place for renewals. During the prior examination, it was suggested that the company include photos of the insured properties with their policy file and that this step be included in the inspection procedure for both new and renewal business. During the current examination it was noted that the company has included photos of the new business in the policy files; however, as there are no inspection procedures in place for renewals, no pictures were found in the policy files of renewal business. It is recommended that the company establish a written inspection procedure for renewal business, whereby renewal business is inspected on a sample basis by members of the board of directors who are independent of the risk under consideration, and that the company consider whether the taking of photographs should be included as part of this procedure.

During the examination it was noted that the largest risk was incorrectly reported on the general interrogatories of the annual statement. The company reported $1,141,900 as its gross maximum loss for its largest risk; this risk includes several locations and consequently it is not the maximum fire loss in a single location. In addition, the company reported $265,475 as its excess reinsurance when the maximum reinsurance excess of loss recoverable is $130,000 for a particular risk. The largest risk should have been disclosed as follows:

Gross maximum loss	$880,000
Pro-rata reinsurance	660,000
Net before excess reinsurance	220,000
Excess reinsurance (Classes C-1 and C-2)	130,000
Net exposure	$ 90,000

It is recommended that the company report its largest risk in the general interrogatories in accordance with the Town Mutual Annual Statement Instructions.

Claims Adjusting

The company has an adjusting committee consisting of at least three directors as required by s. 612.13 (4), Wis. Stat. The function of this committee is to adjust or supervise the adjustment of losses.

Accounts and Records

The examiners' review of the company's records indicated that the company is in compliance with s. Ins 13.05, Wis. Adm. Code, which sets forth the minimum standards for the handling of cash and recording of cash transactions by town mutual insurance companies. The examiners noted the following:

1. A proper policy register is maintained
2. A proper cash receipts journal is maintained
3. A proper cash disbursements journal is maintained
4. A proper general journal is maintained
5. A proper general ledger is maintained

An extensive review was made of income and disbursement items. Cash receipts were traced from source records and the proper recording and eventual deposit thereof ascertained. Negotiated checks issued during the period under examination were reviewed, checked for proper endorsement, and traced to cash records. The verification of assets and determination of liabilities were made as of December 31, 2004.

The examiners noted that the company's treasurer has access to the mail, cash receipts and disbursements, and that he performs the accounting and reconciliation of the bank account. It is a sound accounting control procedure to segregate the duties of signing checks and handling cash from those performing accounting functions and reconciling month-end bank balances. Due to the company's limited staffing, the diversification of cash management responsibilities is not ideal. However, the company's manager indicated that bank reconciliations could be reviewed from time-to-time by members of the board of directors. It is recommended that the company's board of directors establish procedures for the review of bank reconciliations from time to time by members of the board of directors.

The company is not audited annually by an outside public accounting firm.

EDP Environment

Company personnel were interviewed with respect to the company's electronic data processing environment. The company does not use computers to process its data.

Business Continuity Plan

A business continuity plan identifies steps to be performed by a company in the event of business interruptions including, but not limited to, the inability to access its computer, the loss of information on its computer, the loss of a key employee, or the destruction of its office building. The company has developed a business continuity plan which appears to be adequate.

Invested Assets

Section 610.23, Wis. Stat., requires insurers to hold all investments and deposits of its funds in its own name except that:

(1) Securities kept under a custodial agreement or trust arrangement with a bank or banking and trust company may be issued in the name of a nominee of the bank or banking and trust company; and

(2) Any insurer may acquire and hold securities in bearer form.

For securities not held under a custodial agreement or trust arrangement with a bank or banking and trust company, s. Ins 13.05 (4), Wis. Adm. Code, requires that:

> Non-negotiable evidences of company investments such as registered bonds, certificates of deposits, notes, etc., shall be maintained in a safe or vault with adequate safety controls or in a safety deposit box in a bank. Negotiable evidences of company investments shall be maintained in a safety deposit box in a bank. Access to a company safety deposit box containing negotiable securities shall require the presence and signature of at least 2 officers, directors or employees of the company.

The company is in compliance with these requirements.

Investment Rule Compliance

The investment rule for town mutual insurers allows a company to invest in common stocks, common stock mutual funds, and other higher risk investments (referred to as “Type 2”) provided that the town mutual has a sufficient amount of lower risk investments (referred to as “Type 1”). A town mutual may invest in Type 2 securities only if it already has sufficient Type 1 investments. Type 1 investments must equal or exceed the greater of items 1, 2, or 3.

1.	Liabilities plus $300,000	$ 511,199
2.	Liabilities plus 33% of gross premiums written	339,553
3.	Liabilities plus 50% of net premiums written	315,958
4.	Amount required (greater of 1, 2, or 3)	511,199
5.	Amount of Type 1 investments as of 12/31/2004	352,436
6.	Excess or (deficiency)	$(158,763)

The company does not have sufficient Type 1 investments.

The investment rule prescribes that a town mutual shall divest any investment which does not comply with the rule within three years of its noncompliance, unless the commissioner permits a longer period or requires a shorter period. Currently the company has Type 2 investments in common and preferred stocks with a statement value of $95,903. These Type 2 investments consist of $40,000 in Wisconsin Reinsurance Corporation preferred stock, $50,924 in Wisconsin Reinsurance Corporation common stock and $4,979 in NAMIC Insurance Company common stock. In March of 1997 the company received permission from this office to keep these investments under the investment rule.

ASSETS

Cash and Invested Cash **$352,436**

The above asset is comprised of the following types of cash items:

Cash deposited in banks-checking accounts	$ 87,436
Cash deposited in banks at interest	265,000
Total	$352,436

Cash deposited in banks subject to the company's check and withdrawal consists of one account maintained in a local bank. Verification of checking account balances was made by obtaining confirmations from the depository and reconciling the amounts shown thereon to company records.

Cash deposited in banks represents the aggregate of ten deposits in six depositories. Deposits were verified by an actual count and inspection of certificates and/or passbooks. Interest received during the year 2004 totaled $11,943. Rates of interest earned on cash deposits ranged from 1.99% to 3.45%. Accrued interest on cash deposits totaled $6,083 at year-end.

Stocks and Mutual Fund Investments **$95,903**

The above asset consists of the aggregate market value of stocks held by the company as of December 31, 2004. Stocks owned by the company are located in a bank safety deposit box, with the exception of the NAMIC Insurance Company common stock. During the prior examination it was determined that the company did not retain any evidence of ownership regarding the NAMIC Insurance Company stock, and it was recommended that the company retain all stock certificates or other evidence of ownership. The company has complied with this prior exam recommendation as a copy of the NAMIC Insurance Company stock certificate was made available for inspection during the current examination.

Stock certificates were physically examined by the examiners. Stock and mutual fund sales for the period under examination were checked to brokers' invoices and advices. The company's investment in stocks and mutual funds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Dividends received during 2004 on stocks and mutual funds amounted to $2,979 and were traced to cash receipts records.

Book Value of Real Estate **$34,948**

The above amount represents the company's investment in real estate as of December 31, 2004. The company's real estate holdings consisted of a home office building located at 265 South Main Street, Cedar Grove, Wisconsin.

The required documents supporting the validity of this asset were reviewed and were in order. Adequate hazard insurance was carried on the real estate and contents as noted under the caption, "Fidelity Bond and Other Insurance." The company's investment in real estate and related items was in conformance with the Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers. Real estate depreciation is calculated using the straight line method.

The company has a written lease agreement with one tenant and rental income received during 2004 was traced to cash receipts records.

Premiums, Agents' Balances in Course of Collection **$21,461**

This asset represents the amounts due from agents or policyholders which are not in excess of 90 days past due at year-end. A reclassification of $4,830 was made to this line item to properly report those premiums with multiple installments that were not yet due at year-end. A review of the agent/agency statements and subsequent payments verified this balance.

Premiums Deferred and Not Yet Due **$4,830**

This asset represents modal premium installments (such as monthly, quarterly, etc.) that are not yet due. A review of the policy register indicated that the company had six policies with semi-annual mode of payment due from July to December of 2004 and one policy due in August which was paid in three installments; therefore, a reclassification to decrease the Premiums in Course of Collection balance was made to properly report deferred premiums. The prior examination recommended that the company calculate and record deferred premiums in accordance with the Town Mutual Annual Statement Instructions. The company has not complied with this prior exam recommendation. It is again recommended that the company calculate and record deferred premiums in accordance with the Town Mutual Annual Statement Instructions.

Investment Income Accrued **$6,083**

Interest due and accrued on the assets of the company at December 31, 2004, is entirely related to accrued interest on certificates of deposit in the amount of $6,083.

Reinsurance Commission Receivable **$4,960**

The examination resulted in an adjustment to increase the Reinsurance Commission Receivable balance to reflect the profit commission due from the reinsurer at year-end; and, consequently, Policyholders' Surplus was increased by $4,960.

Furniture and Fixtures **$0**

This asset consists of $3,541 of furniture and office equipment owned by the company at December 31, 2004. In accordance with annual statement requirements, this amount has been reported as a nonadmitted asset, and thus the balance shown above is $0. This balance was increased by $997 in 2004 due to acquisition of a new photocopy machine.

Prepaid Expenses **$0**

This asset consists of prepaid insurance for the company. A review of the policies and paid invoices verified this asset. In accordance with annual statement instructions, this amount of $453 has been reported as a nonadmitted asset.

LIABILITIES AND SURPLUS

Net Unpaid Losses **$8,580**

This liability represents losses incurred on or prior to December 31, 2004, that remained unpaid as of that date. The examiners reviewed the reasonableness of this liability by totaling actual loss payments made subsequent to December 31, 2004, with incurred dates in 2004 and prior years. To the actual paid loss figure was added an estimated amount for 2004 and prior losses remaining unpaid at the time of the examination. The examiners' development of unpaid losses is compared with the amount estimated by the company in the following schedule.

	Company Estimate	Examiners' Development	Difference
Incurred but unpaid losses	$42,007	$38,346	$3,661
Less: Reinsurance recoverable on unpaid losses	33,427	30,804	2,623
Net Unpaid Losses	$ 8,580	$ 7,542	$1,038

The above difference of $1,038 was not considered material for purposes of this examination.

The examiners' review of claim files included open claims, paid claims, claims closed without payment, and claims which were denied during the examination period. The review indicated that claims are investigated and evaluated properly and that payments are made promptly and in accordance with policy provisions upon the submission of a proper proof of loss. In addition, the review of claims handling procedures and files revealed the following:

1. A proper loss register is maintained.
2. Claim files contained sufficient investigatory data and documentation to verify settlement payments or reserve estimates.
3. Proofs of loss were properly signed.

During the prior examination it was recommended that the company record all reinsurance recoverables in the loss register and in the claim files. The company continues not to register reinsurance recoverables in the loss register; however, copies of the recoveries were found on all the claim files of the selected samples, when applicable. Examiners were able to verify the amounts of recoveries from the reinsurer; therefore, the company has adequately complied with the prior exam recommendation.

Unpaid Loss Adjustment Expenses **$600**

This liability represents the company's estimate of amounts necessary to settle losses that were incurred prior to December 31, 2004, but which remained unpaid as of year-end. The methodology used by the company in establishing this liability is not reasonable.

The examiners' analysis of expenses incurred in the current year related to the settlement of prior year losses, as well as estimates of amounts necessary to settle any prior losses remaining unpaid at the examination date, indicated that this liability was overstated; however, the methodology utilized by the company does not appear reasonable. The company has been reporting a fixed amount of unpaid loss adjustment expenses during the years under examination; the estimated liability is not related to the number of open claims nor to the cost of settling those claims. No adjustment to increase policyholders' surplus was made since the overstatement is below tolerable error. It is again recommended that the company establish a logical methodology in determining unpaid loss adjustment expenses.

Commissions Payable **$3,760**

This liability represents the commissions payable to agents as of December 31, 2004. The examiners reviewed the company's commission calculation and subsequent commission payments and found the liability to be reasonably stated.

Fire Department Dues Payable **$239**

This liability represents the fire department dues payable to the State of Wisconsin as of December 31, 2004. The examiners reviewed the company's fire department dues calculation and found this liability to be correctly calculated. The actual amount paid was verified to the cash disbursement records.

Unearned Premiums **$187,755**

This liability represents the reserve established for unearned premiums in compliance with s. Ins 13.08 (3), Wis. Adm. Code. The reserve established was 50% of the premiums in force, net of the premiums ceded to the reinsurer.

Reinsurance Payable **$2,848**

This liability consists of amounts due to the company's reinsurer at December 31, 2004, relating to transactions which occurred on or prior to that date. Subsequent cash disbursements and reinsurer accounting records indicated that the company overstated this liability by $3,200. The Reconciliation of Policyholders' Surplus section of this report reflects the examiners' adjustment to decrease the Reinsurance Payable balance and thereby increase policyholders' surplus by $3,200.

Amounts Withheld for the Account of Others **$1,094**

This liability represents employee payroll deductions in the custody of the company on December 31, 2004. Supporting records and subsequent cash disbursements verified this item.

Payroll Taxes Payable **$305**

This liability represents the company's portion of payroll taxes incurred prior to December 31, 2004, which had not yet been paid. Supporting records and subsequent cash disbursements verified this item.

Accounts Payable **$210**

This liability represents the company's general accounts payable incurred prior to December 31, 2004, which had not been paid as of year-end. The examiners verified this balance by reviewing the invoices to the subsequent payments and determined that this liability was correctly stated.

Accrued Property Taxes **$2,608**

This liability represents property taxes accrued at year-end on the real estate and personal property owned by the company. The balance was verified by reviewing the property tax bills to the subsequent payment.

V. CONCLUSION

As of December 31, 2004, the company reported assets of $515,661, liabilities of $211,199, and surplus of $304,462. As a result of this examination, two adjustments were made totaling $8,160 which increased surplus to $312,622. In addition, one reclassification of $4,830 was made to properly record deferred premiums.

During the four years under examination, surplus decreased 19% due to the cumulative net losses since 2001. In 2004, the company experienced its first positive net underwriting income in the last ten years and its first net income during the period under examination. Underwriting income in 2004 was $15,640 and net income was $36,832. Net premiums written increased 68% since 2001 and policies in force also increased 12% during the same period.

The company's net underwriting expense ratio has been as high as 36 percentage points greater than the average for the Wisconsin town mutual industry as a whole in 2001 and during the period under examination it has averaged 25 percentage points greater than the Wisconsin town mutual average. In 2004, the company was 12 percentage points over the average, which indicates improvement, but this improvement will need to be continued and sustained for the company to continue independently.

This examination resulted in five recommendations, including two recommendations from the prior examination report with which the company did not comply and one recommendation with which partial compliance was noted. Areas of improvement recommended by this examination included inspection procedures, risk disclosure, bank reconciliation procedures, recording of deferred premiums, and reserving for loss adjustment expenses.

VI. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 16 - Underwriting—It is recommended that the company establish a written inspection procedure for renewal business, whereby renewal business is inspected on a sample basis by members of the board of directors who are independent of the risk under consideration, and that the company consider whether the taking of photographs should be included as part of this procedure.

2. Page 16 - Underwriting—It is recommended that the company report its largest risk in the general interrogatories in accordance with the Town Mutual Annual Statement Instructions.

3. Page 17 - Accounts and Records—It is recommended that the company's board of directors establish procedures for the review of bank reconciliations from time to time by members of the board of directors.

4. Page 22 - Premiums Deferred and Not Yet Due—It is again recommended that the company calculate and record deferred premiums in accordance with the Town Mutual Annual Statement Instructions.

5. Page 24 - Unpaid Loss Adjustment Expenses—It is again recommended that the company establish a logical methodology in determining unpaid loss adjustment expenses.

VII. ACKNOWLEDGMENT

The courteous cooperation extended to the examiners by the company's personnel is hereby acknowledged.

In addition to the undersigned, Angela Graff of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination.

Respectfully submitted,

Carina Toselli
Examiner-in-Charge